

Message Text

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ACTION EUR-12

INFO OCT-01 EA-10 ISO-00 AID-05 CIAE-00 COME-00 EB-08
FRB-03 INR-10 NSAE-00 ICA-11 XMB-02 OPIC-03 SP-02
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/097 W

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R 231826Z MAY 78
FM AMEMBASSY BONN
TO SECSTATE WASHDC 8799
DEPARTMENT TREASURY
INFO WHITE HOUSE WASHDC
AMEMBASSY BRUSSELS
AMEMBASSY PARIS
AMEMBASSY TOKYO
AMEMBASSY ROME
AMEMBASSY OTTAWA
AMEMBASSY LONDON

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WHITE HOUSE FOR OWEN: USOECD ALSO FOR EMBASSY, USEEC

E.O. 11652: N/A
TAGS: ECON EFIN GW
SUBJECT: BERLIN ECONOMIC INSTITUTE WANTS MORE
ATTENTION TO GROWTH AND LESS TO INFLATION

REF: BONN 7454

1. SUMMARY -- BERLIN ECONOMIC INSTITUTE URGES FASTER
PACE OF GOVERNMENT INVESTMENT TO COMBAT UNEMPLOYMENT;
BELIEVES CONTINUED FRG PREOCCUPATION WITH INFLATION
IS BAD POLICY FROM BOTH DOMESTIC AND INTERNATIONAL
VIEWPOINTS. END SUMMARY.

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2. EMBASSY ECONOFF AND TREASURY DESKOFF FOR FRG
VISITED GERMAN ECONOMIC RESEARCH INSTITUTE (DIW) AND
DISCUSSED ECONOMIC POLICY ISSUES WITH STAFF RESPONSIBLE
FOR ECONOMIC FORECASTING, FOREIGN TRADE, AND EXCHANGE
RATES. AS REPORTED IN REFTEL, DIW HAS BEEN STRONGLY
PROMOTING HIGHER VOLUME OF GOVERNMENT INVESTMENT TO
COMBAT UNEMPLOYMENT. IN TALKS WITH US HEAD OF DIW

FORECASTING DEPARTMENT INDICATED THAT DIW PRIVATELY BELIEVES A MODERATE BOOST IN GOVERNMENT SPENDING (PRIMARILY INVESTMENT) WOULD BE A REALISTIC OBJECTIVE OF ECONOMIC POLICY, RATHER THAN THE MORE AMBITIOUS TARGETS CALLED FOR IN ITS PUBLISHED STUDY. THIS WOULD INVOLVE A CONTINUATION OF THE DM 16 BILLION INVESTMENT PROGRAM BUT WITH EXPENDITURES AT A RATHER MORE RAPID PACE (NOW MOSTLY OVER A TWO YEAR PERIOD), AND SOMEWHAT FASTER EXPANSION OF GOVERNMENT CONSUMPTION.

3. DIW DOES NOT ACCEPT ARGUMENTS ABOUT THE INFLATIONARY CONSEQUENCES OF THESE PROPOSALS FROM OPPONENTS OF HIGHER GOVERNMENT SPENDING. AS DIW SEES IT, THE GERMAN ECONOMY CAN MORE COMFORTABLY LIVE WITH A THREE PERCENT RATE OF INFLATION THAN IT CAN WITH A HIGHER RATE OF UNEMPLOYMENT, WHICH IS WHAT IT WILL HAVE IF GOVERNMENT DOES NOT TAKE A MORE ACTIVE ROLE IN CREATING JOBS FOR MUCH EXPANDED WORKFORCE IN PERIOD 1979-1988. MOREOVER, THE ONLY WAY TO TEST LABOR MARKET SLACK IS TO CREATE ADDITIONAL DEMAND AND SEE WHAT HAPPENS TO WAGE COSTS. DIW WOULD FAVOR ADMISSION OF MORE GUEST WORKERS TO EASE LABOR SUPPLY BOTTLENECKS IN PARTICULAR INDUSTRIES (E.G., IN CONSTRUCTION INDUSTRY WHERE GERMAN LABOR REPUTEDLY IS RELUCTANT TO ACCEPT EMPLOYMENT) IF THIS WOULD FACILITATE OVERALL EXPANSION.

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4. IN DIW'S VIEW, IT WOULD NOT BE SUCH A BAD THING IF SUCH A PROGRAM PREVENTED A FURTHER DECREASE IN THE RATE OF INFLATION. CONVERGENCE OF INFLATION AND GROWTH

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RATES AMONG PRINCIPAL TRADING COUNTRIES WOULD
HELP SETTLE EXCHANGE RATE MARKETS AND THEREBY LIFT
BUSINESS CONFIDENCE.

5. DIW IS MILDLY OPTIMISTIC THAT FINANCE MINISTER'S
RECENT REMARKS ABOUT AN EXPANSIONARY 1979 BUDGET INDICATE
SOME MOVEMENT BY THE GOVERNMENT TOWARD THE DIW POSITION.
DIW OPPOSES A TAX CUT (AN APPROACH LOOKED UPON WITH
GREATER FAVOR BY ECONOMICS MINISTER LAMBSDORFF)
ARGUING THAT THERE IS NO WAY OF KNOWING HOW THE
ADDITIONAL INCOME WOULD BE USED WHEREAS GOVERNMENT CAN
DIRECT ITS EXPENDITURES TO OBTAIN THE GREATEST ECONOMIC
IMPACT.

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6. AS FOR 1978 PERFORMANCE OF THE ECONOMY, DIW BELIEVES
MUCH WILL HINGE ON COURSE OF DM/DOLLAR EXCHANGE RATE.
IF DOLLAR CONTINUES TO APPRECIATE, EXPORTS SHOULD
PERFORM BETTER THAN 3 1/2 PERCENT GROWTH RATE
ESTIMATED BY DIW AND MANY OTHER FORECASTERS. INVESTMENT
WOULD ALSO BE ENCOURAGED. ECONOMY WILL ALSO GET SOME
IMPETUS FROM LATE 1977 ENACTED PROGRAM FOR TAX RELIEF
AND INCREASED EXPENDITURES. DIW SEES FIRST QUARTER
GNP (SEASONALLY AND WORKDAY ADJUSTED BASIS) DOWN BY
ABOUT 1/2 PERCENT FROM FOURTH QUARTER 1977. STRIKES,
BAD WEATHER, AND EXCHANGE RATE DISTURBANCES, THEY
ESTIMATE, MEANT A LOSS OF ABOUT ONE PERCENT OF GNP
DURING FIRST QUARTER, OF WHICH ABOUT HALF SHOULD BE
MADE UP DURING REST OF 1978.

7. COMMENT -- MATTHOEFER'S RECENT PUBLIC UTTERANCES
APPEAR TO PROMISE A FISCAL BOOST FOR 1979, BUT NOT
NECESSARILY BY NEARLY SO MUCH AS FAVORED BY DIW. ALSO
GOVERNMENT ECONOMIC ANALYSTS ARE SAYING THAT FIRST
QUARTER MAY NOT TURN OUT AS BADLY AS DIW AND OTHERS
THINK DESPITE BAD FIRST QUARTER INDUSTRIAL PRODUCTION
FIGURES. IF THEY ARE RIGHT, ARGUMENTS AGAINST LARGE
NEW ECONOMIC PROGRAM WILL CARRY GREATER FORCE.
STOESSEL

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